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EX PARTE OR LATE FILED

February 26, 2001

Ms. Dorothy Attwood
Chief, Common Carrier Bureau
Federal Communications Commission
445 12th Street, SW, 5th Floor
Washington, DC 20554

Re: ***Ex Parte*** **Communication**
ISP Declaratory Ruling Remand/
Inter-Carrier Compensation for ISP-Bound Traffic
CC Docket Nos. 96-98, 99-68

Dear Ms. Attwood:

This *ex parte* communication, submitted on behalf of the Association for Local Telecommunications Services ("ALTS") and the Competitive Telecommunications Association ("CompTel"), responds to assertions made by incumbent local exchange carriers ("ILECs") that the Federal Communications Commission ("FCC" or "Commission") legally could mandate "bill and keep" for the transport and termination of calls to Internet Service Providers ("ISP-bound traffic").[1] As demonstrated below, under either Sections 251/252 or 201(b), the Commission may not impose a confiscatory inter-carrier compensation mechanism, as bill-and-keep would be in the case of materially out-of-balance ISP-bound traffic, without violating the Communications Act of 1934, as amended (the "Act") and the takings clause of the Fifth Amendment to the United States Constitution.

[1] Pursuant to 47 C.F.R. § 1.419(b), an original and one copy have been submitted to the Secretary of the Commission.

In response to the remand by the United States Court of Appeals for the District of Columbia Circuit, the Commission first must explain why ISP-bound traffic is (or, as the Court appeared to indicate, is not) telecommunications traffic that somehow falls outside the scope of the reciprocal compensation requirement of Section 251(b)(5). As the undersigned parties have argued in prior filings in this docket, the Court's decision and the provisions of the Act essentially bar such a result. ISP-bound traffic fits within the model of local calling. Moreover, it does not fit the Act's definition of "exchange access" and it is not subject to access charges. Indeed, none of the putative justifications for exempting access traffic from reciprocal compensation exist with respect to ISP-bound traffic.[2] Nevertheless, in response to ILEC arguments to the contrary, the undersigned parties set forth below the legal basis for their jointly held position that the Commission does not have the legal authority under Sections 251/252 *or 201(b)* for establishing a mandatory bill-and-keep non-compensation mechanism for the transport and termination of materially out-of-balance traffic.

The Plain Language of Section 252(d)(2) Bars the Imposition of Mandatory Bill-and-Keep for ISP-Bound Traffic

In the case of ISP-bound traffic, where the exchange of traffic between local exchange carriers ("LECs") typically is materially out-of-balance, Section 252(d)(2) plainly bars the mandatory application of bill-and-keep in lieu of cost-based reciprocal compensation required under Section 251(b)(5). To be sure, Section 252(d)(2) permits "arrangements that *afford the mutual recovery of costs through the offsetting of reciprocal obligations,* including arrangements that waive mutual recovery (such as bill-and-keep arrangements)." *Id.* § 252(d)(2)(B)(i) (emphasis added). However, as the Commission correctly concluded in its 1996 *Local Competition Order,*[3] the FCC's and the states' authority to impose mandatory bill-and-keep is *limited* by the plain language of Section 252(d)(2): the reciprocal obligations must be *offsetting* – "the volume of terminating traffic that originates on one network and terminates on another network [must be] approximately equal to the volume of traffic flowing in the opposite direction, and [must be] expected to remain so." *Local Competition Order,* ¶ 1111.

In that same 1996 *Local Competition Order,* the Commission recognized that:

> Section 252(d)(2)(A)(i) provides that to be just and reasonable, reciprocal compensation *must* "provide for the mutual and reciprocal recovery by each carrier of costs associated with transport and termination",

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[2] Notably, although exchange access traffic is not currently subject to reciprocal compensation, it is subject to compensation at rate levels that generally are much higher than the cost-based rates that the states have established for reciprocal compensation.

[3] *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 11 FCC Rcd 15499 (rel. Aug. 8, 1996) (*"Local Competition Order"*) (subsequent history omitted).

id., ¶ 1112 (emphasis added), and correctly concluded that:

> carriers incur costs in terminating traffic that are not *de minimis*, and consequently, bill-and-keep arrangements that lack any provisions for compensation do not provide for recovery of costs. . . . We conclude, therefore that states may impose bill-and-keep arrangements if traffic is roughly balanced in the two directions . . . ."

Id. Thus, the Commission also correctly concluded that:

> If state commissions impose bill-and-keep arrangements, those arrangements *must* either include provisions that impose compensation obligations if traffic becomes significantly out of balance or permit any party to request that the state commission impose such compensation obligations based on a showing that the traffic flows are consistent with the threshold adopted by the state.

Id. (emphasis added).

The Commission also addressed the takings issue raised by the imposition of mandatory bill-and-keep. Specifically, the Commission noted that *provided that reciprocal compensation obligations were offsetting* (*i.e.*, traffic volumes exchanged are approximately equal) the imposition of mandatory bill-and-keep would not be unconstitutionally confiscatory. *Id.*, ¶1116. From this language, it fairly can be implied, that the Commission itself understood that, absent the *statutory* proviso that obligations must be *offsetting*, mandatory bill-and-keep/zero-rated reciprocal compensation would indeed be unconstitutionally confiscatory. The Commission's 1996 conclusions remain sound.

Indeed, the language of Sections 251(b)(5) and 252(d)(2) has not changed since 1996. Nothing in the record suggests that the Commission misinterpreted these provisions in its 1996 *Local Competition Order.* Nothing has transpired to adjust this statutory framework carefully crafted by Congress to avoid a takings (an unconstitutional one, in the case of confiscatory rate setting). The Fifth Amendment also remains unchanged. Takings without compensation are unconstitutional.[4]

In sum, the Commission already correctly has concluded that Sections 251/252 neither contemplate nor authorize the imposition of mandatory bill-and-keep for the exchange of telecommunications traffic that would not be approximately equal in both directions. Since 1996, no lawful basis for overturning this precedent has been created.

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4 *E.g.*, *Oklahoma-Arkansas Tel. Co. v. Southwestern Bell Tel. Co.*, 45 F.2d 995 (8th Cir. 1930), *cert. denied*, 283 U.S. 822 (1931)(mandatory interconnection constitutes a taking and therefore requires compensation) (*"Oklahoma-Arkansas Tel."*).

Section 201(b) Does Not Authorize the Commission to Engage in Confiscatory Rate Making

Recently, the ILECs have argued that the Commission may mandate bill-and-keep or zero-rated compensation pursuant to Section 201(b). Their arguments are completely without merit. Even assuming that ISP-bound traffic somehow lawfully could be carved out of the Section 251(b)(5) requirement that reciprocal compensation be paid for the transport and termination of *telecommunications* (which it cannot), Section 201(b) still requires that rates "shall be just and reasonable".[5] Moreover, Section 201(b) does not insulate the Commission from the Fifth Amendment's bar on uncompensated takings.

Even under Section 201(b), rates must be established to permit interconnecting carriers the ability to recover costs.[6] The Commission already has determined that the costs of transport and termination are not *de minimis. Local Competition Order,* ¶ 1112; *see also Inter-Carrier Compensation for ISP-Bound Traffic,* CC Docket 99-68, Notice of Proposed Rule Making, ¶ 29 ("We acknowledge that, no matter what the payment arrangement, LECs incur a cost when delivering traffic to an ISP that originates on another LEC's network."). Even the most recent ILEC cost studies and state commission-approved rates confirm that the costs for the transport and termination of ISP-bound traffic are not *de minimis.*[7] Thus, where costs are incurred, as the Commission already has determined is the case when telecommunications traffic is transported and terminated to ISPs, a zero rate (*i.e.,* mandatory bill-and-keep) does not meet the Section 201(b) requirement that rates "shall be just and reasonable".

ILEC assertions that competitive local exchange carrier ("CLEC") costs are somehow below their own TELRICs defy logic. The ILECs' TELRIC studies already should reflect the costs associated with the most efficient technology and network configuration available. As a result of the ILECs' successful attack on the FCC's TELRIC pricing methodology, under the Eighth Circuit's view of the cost inputs that are appropriate for the TELRIC costing methodology (cost inputs should be those for equipment actually used, rather than those for the most efficient equipment available), reciprocal compensation rates set using cost inputs for the most efficient equipment available may result in reciprocal compensation rates that are

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5 *See, e.g., Bell Atl. Tel. Cos. v. FCC,* 24 F.3d 1441, 1445-46 (D.C. Cir. 1994)(the FCC shall construe the Communications Act in a manner so as to avoid raising claims of unconstitutional takings).

6 *See, id., see also Oklahoma-Arkansas Tel.* 283 U.S. 822.

7 For example, both the New York and Texas Commissions recently examined the costs associated with the transport and termination of ISP-bound traffic and found that the costs associated were not *de minimis. See e.g., Proceeding on Motion of the Commission to Reexamine Reciprocal Compensation,* Case No. 99-C-0529, 1999 WL 1020550, Opinion and Order Concerning Reciprocal Compensation (NY PSC Aug. 26, 1999) (establishing a 3:1 traffic imbalance ratio, beyond which all local traffic – including ISP-bound traffic – will be compensated at end office rates rather than tandem rates); *Proceeding to Examine Reciprocal Compensation Pursuant to Section 252 of the Federal Telecommunications Act of 1996,* Docket No. 21982, Revised Arbitration Award (TX PUC Aug. 14, 2000)(establishing a bifurcated end office rate, a composite tandem-served rate and a 3:1 traffic imbalance ratio applicable to all local traffic, including ISP-bound traffic).

unlawfully low.[8] Notably, the record in this proceeding makes clear that CLECs typically use the same switching equipment for ISP-bound traffic as they do for all other local traffic. Thus, CLECs typically incur the same costs regardless of whether the traffic is local voice traffic or local ISP-bound traffic.

Tacitly recognizing that cost recovery is necessary, even under Section 201(b), ILECs have argued that CLECs recover the costs of transport and termination of ISP-bound calls from ISPs. Here, too, the ILECs' arguments are without merit. Like all local calling, ISP-bound traffic is "sent-paid" traffic. Under the sent-paid model, costs of transport and termination are recovered from the originating party and, in a two carrier scenario, from the carrier serving the originating party.[9] Costs are not recovered from the recipient of the call. Thus, under the sent-paid model, inter-carrier compensation is the means by which an unconstitutional taking of the terminating carrier's property is avoided. Nothing in the record, or in Section 201(b), suggests that there is a sound basis for upending the sent-paid model with respect to local calls transported and terminated to ISPs.[10]

Thus, because ISP-bound traffic is "sent-paid" and the costs of transport and termination for ISP-bound traffic are not *de minimis*, the exchange of such traffic between LECs will result in a taking of the terminating LEC's property, if the originating LEC is permitted to avoid compensating the terminating LEC via mandatory bill-and-keep. It is well established that the failure of a carrier to compensate another adequately for the required use of its facilities is confiscatory.[11] Section 201(b) provides no more insulation from the Fifth Amendment Takings Clause than do Sections 251 and 252. Indeed, mandatory bill-and-keep for ISP-bound traffic would constitute a takings under any section of the Communications Act.

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8 *Iowa Utils. Bd. v. FCC,* 219 F.3d 744, 749-51 (8th Cir. 2000), *partial stay granted* (Sept. 22, 2000), *and cert. granted sub nom. Verizon Communications et al. v. FCC et al.*, 121 S. Ct. 877 (2001).

9 ILEC claims that they do not adequately recover from their originating end users the costs of ISP-bound traffic are unsubstantiated. Moreover, as the Commission recognized in the past, ILEC claims of under-recovery should be presented to the relevant state commissions. *Access Charge Reform,* First Report and Order, 12 FCC Rcd 15982, ¶ 346 (1997) ("To the extent that some intrastate pricing structures fail to compensate incumbent LECs adequately for providing service to customers with high volumes of incoming calls , incumbent LECs may address their concerns to state regulators.").

10 *See, e.g, Intermedia, KMC, e.spire, Time Warner, Focal Ex Parte,* CC Docket No. 99-68 (Nov. 30, 2000).

11 *See Smith v. Ill. Bell Tel. Co.,* 282 U.S. 133, 160-161 (1930) (reducing rates for services rendered below a point at which a utility is able to make a "fair return on the value of the property" used by a second utility rises to levels of confiscation of the first utility's property).

For all of the foregoing reasons, the Commission should decline the ILECs' requests for it to adopt an unlawful mandatory bill-and-keep mechanism for ISP-bound traffic. For traffic that is materially out-of-balance, as ISP-bound traffic tends to be, mandatory bill-and-keep would violate the statutory language of either Sections 251/252 or 201(b) and would amount to a takings unauthorized by any section of the Communications Act and in violation of the Fifth Amendment of the United States Constitution.

Respectfully submitted,

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